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IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

GENERAL ELECTRIC COMPANY, and
DRUCKER & GENUTH, MDs, P.C., d/b/a
SOUTH SHORE IMAGING ASSOCIATES,
Petitioners,

v.

FONAR CORPORATION and
DR. RAYMOND V. DAMADIAN,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

REPLY BRIEF OF PETITIONER

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REPLY BRIEF OF PETITIONER

This case raises two fundamental legal questions that dictate both the outcome of patent litigation and the financial importance of such cases on a daily basis. More than 100 years ago this Court adopted the rule that an infringer of an improvement patent is liable only for the value of the improvement unless that improvement is essential to the sale of the entire machine. The Federal Circuit's departure from that rule has dramatically increased the stakes of patent litigation by dangling extraordinary windfalls before plaintiffs and their attorneys. Respondents make no effort to dispute the vital role the entire market value rule ought to play in preventing such windfalls, choosing instead to mischaracterize the Court's precedents.

Concomitantly, the random refusal of panels of the Federal Circuit to require particularized testimony and linking argument further compounds the black-box jury verdict problem that has long plagued the use of the doctrine of equivalents. The absence of this essential procedural protection, which is precisely the kind of limitation this Court called for in *Hilton-Davis* (see Pet. 17), plainly impairs the ability of businesses to bring new products to market for fear that years later the Federal Circuit will permit an infringement verdict to be upheld on a theory of equivalence never even presented to the jury. Because such a verdict may now carry with it a price tag that is 100 or even 1,000 times greater than any damages based strictly on the value of the improvement, the threat to innovation has become extraordinary.

Nowhere do respondents dispute these vital propositions that demand the attention of this Court. Instead, respondents primarily assert that this Court's entire market value rule was limited to cases involving a now-obsolete form of damages calculations—an unprecedented assertion that is demonstrably false. The legal questions presented embody " 'the most profound departure[s] from basic patent law concepts that any court has ever pronounced' " (see Pet. 17 (citation omitted)) and nothing in respondents' opposition negates that conclusion.

I.

In the petition for certiorari, GE demonstrated that the test used by the Federal Circuit in this case and in other cases for determining whether a patent on one feature of a machine entitles a patentee to recover damages based on the value of the whole machine is irreconcilable with the "entire market value rule" set forth by this Court over a century ago and enforced for decades afterwards by the courts of appeals. GE further demonstrated that application of the original rule would have required reversal of the damages awarded below.

Fonar responds chiefly with a diversionary tactic: It claims that this conflict is "wholly illusory" because this Court's precedents concerned disgorgement of the *infringer's* profits, not recovery of the patent holder's lost profits or reasonable royalties. Opp. 8-10. Fonar's assertion is simply wrong.

This Court developed and applied the entire market value rule to claims for *both* disgorgement of the defendant's profits [1] *and* for recovery of the patentee's own lost profits.[2] Thus, it is entirely irrelevant that, as Fonar repeatedly asserts, "[t]he whole profits from *GE*'s MRI machines were not requested by Fonar, were not awarded by the jury, and were not approved as damages by the

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[1] *E.g.*, *Seymour* v. *McCormick*, 57 U.S. (16 How.) 480, 490-91 (1853).

[2] *See Dobson* v. *Hartford Carpet Co.*, 114 U.S. 439, 442-46 (1885) (reversing damages award of "entire profit to the *plaintiffs*" due to "decrease of the *plaintiff's* sales" where only a small part of plaintiff's lost profits consisted of "the value which the [patented] designs contributed") (emphases added); *Dobson* v. *Dornan*, 118 U.S. 10, 17-18 (1886) (overturning an award of "the entire profit which the *plaintiffs* would have received" from the sale of an equal quantity of carpets that defendant sold because there was no evidence to support "the assumption that the whole of [plaintiffs' profit] was due to solely the [patented] design") (emphasis added). If, as Fonar suggests, the entire market value rule did not apply to claims for *plaintiff's* lost profits, there would have been no need for this Court to determine whether the plaintiffs in these cases had satisfied the test.

Federal Circuit." Opp. 7, 9 (emphasis added). GE never suggested otherwise in its petition for the simple reason that this Court's entire market value rule was never limited to claims for disgorgement of the infringer's profits.

For this same reason, Fonar's oblique suggestion that the "1952 patent statute" somehow superseded this Court's entire market value rule (Opp. 9-10) is likewise wrong. The 1952 Act merely recodified amendments Congress passed in 1946, one of which eliminated disgorgement of an infringer's profits as a method of determining damages. See *Aro Mfg. Co.* v. *Convertible Top Replacement Co.*, 377 U.S. 476, 505 n.20 (1964). In so doing, however, Congress did not disturb, let alone nullify, the applicability of the entire market value rule to claims for plaintiff's lost profits or a reasonable royalty, and Fonar cites no case suggesting otherwise. To the contrary, the Federal Circuit itself recently reaffirmed that "[w]hen a patentee seeks damages on unpatented components sold with a patented apparatus, courts have applied a formulation known as the 'entire market value rule' to determine whether such components should be included in the damage computation, *whether for reasonable royalty purposes, . . . or for lost profits purposes.*" *Rite-Hite Corp.* v. *Kelley Co.*, 56 F.3d 1538, 1549 (Fed. Cir.) (*in banc*), *cert. denied*, 116 S. Ct. 184 (1995) (citations omitted) (emphasis added). Thus, Fonar's claim that the Court's prior decisions are irrelevant to "modern [damages] methodology" has never been accepted by any court, including the Federal Circuit, and has no basis in either the statute, this Court's piror cases, or those of lower courts.[3]

Fonar's second claim is that the damages award here comports with the "modern methodology" for calculating damages. Opp. 9-10. But this in no way diminishes the

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[3] Indeed, Fonar never attempts to reconcile its claim that this Court's entire market value rule was limited to the now-defunct remedy of disgorgement of defendant's profits with its claim that the Federal Circuit "appropriately" discussed the rule when analyzing the jury's reasonable royalty award. Opp. 6.

need for certiorari. The Federa Circuit did apply its now-
diluted version of the entire m ket value rule, in which
evidence that a single feature touted as useful in mar-
keting brochures is deemed suf ient to entitle a patentee
to collect damages based on t value of the whole ma-
chine. And it is precisely the c flict between the Federal
Circuit's "modern" version of e rule and this Court's
original formulation that merits his Court's review.

Fonar's defense of the dam es awarded in this case
cannot obscure this conflict. Fo ar incorrectly asserts that
a reasonable royalty award is a ays calculated by apply-
ing a royalty rate to "the pric of the whole machine."
Opp. 12; see *id.* at 10 (royalt is calculated using "the
price of the whole machine as 'base' "). In fact, such a
calculation is proper *only* if the ntire market value rule is
satisfied. See, *e.g., Decca Ltd. United States,* 640 F.2d
1156, 1175 (Ct. Cl. 1980) (npatented items used in
combination with a patented in ntion are to be included
in the royalty base . . . *only if* e invention has substan-
tially created the value of the ms") (emphasis added);
Marconi Wireless Tel. Co. of A erica v. *United States,* 99
Ct. Cl. 1, 49 (1942), *aff'd in art,* 320 U.S. 1 (1943)
(where "the invention was of s h paramount importance
that it substantially created th value of the component
parts . . . [t]he complete cost the transmitting and re-
ceiving sets should be used as e base in the application
of a reasonable royalty"). If t entire market value test
is not satisfied, the reasonable yalty rate must be multi-
plied *not* against "the price of e whole machine" (Opp.
10) but against the value of t patented feature alone.
See, *e.g., Decca Ltd.,* 640 F.2 at 1175 (excluding the
value of land and buildings fro the royalty base for pat-
ented transmitting stations beca e the items "are suscepti-
ble of uses not involving the [i tent]; and their value de-
rives, at least in part, from this otential for other uses").[4]

[4] Indeed, Fonar's argument obviou y proves too much: if it were standard always to multiply the roy y rate times the price of the whole machine, then there would n er be any role even for the diluted "entire market value rule" at the Federal Circuit continues to apply.

The difference is not one of mere semantics: The record is undisputed that Fonar charged only $1,000 extra for this optional patented feature if ordered with a new machine, and $15,000 extra if ordered separately to upgrade an old machine. C.A. App. A5044, A7169. The value of GE's scanners, by contrast, averaged about $1.7 million (C.A. App. A5256), resulting in a damages award vastly greater than this Court's precedents would permit. Thus, had the jury applied its royalty rate of 4 percent (see Opp. 12) against the value of the MAO feature alone, the damages awarded (for the 525 scanners at issue) would have been $315,000 (using the more generous $15,000 cost for upgrades), about one one-hundredth of the $34 million in reasonable royalties that the jury actually awarded.[5]

With respect to lost profits, Fonar's assertion that the entire market value rule is inapplicable is frivolous given the absence of any supporting authority and the Federal Circuit's express confirmation in *Rite-Hite* that the entire market value rule continues to apply—as it has for over a century—to lost profits awards. See *supra* at 2-3. Here, the jury awarded Fonar its entire claimed profit of $371,000 per machine (C.A. App. A5079) for each of the 75 GE sales that the jury concluded Fonar would have made in the absence of GE's infringement. Under the traditional entire market value rule, in the absence of proof that purchasers were "refusing to buy" the "total mechanism" without the patented improvement, Fonar was not "entitled to the profits for the entire value of the total mechanism." *Universal Athletic Sales Co.* v. *American Gym,* 480 F. Supp. 408, 414 (W.D. Pa. 1979); see also *Westinghouse* v. *New York Air Brake Co.,* 140 F. 545, 553 (2d Cir. 1905) (there is "no basis for a recovery" of

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[5] Because the cost of upgrading an existing MRI includes the costs of retrofitting the apparatus, the $15,000 upgrade figure is an undoubtedly inflated measure of the value of the MAO feature. If the $1,000 price that Fonar charged for this option on new machines is used as the royalty base, the award in this case would have been approximately $21,000.

"all of the profits which [plaintiffs] lost" unless plaintiffs show that "without the [patented apparatus], there would have been no market for the other [unpatented] parts"). Again, had the Federal Circuit followed the traditional rule, it could not have approved the jury's award of lost profits to Fonar.

Fonar's remaining arguments are equally unfounded. Having argued that the entire market value rule has been superseded, Fonar then argues inconsistently that there was sufficient evidence in the record to satisfy the rule. Opp. 12-14. Contrary to Fonar's misleading suggestion, however, the Federal Circuit nowhere relied on or even mentioned the supposed "small mountain of . . . technical literature" presented at trial (Opp. 13) and lower courts will not, in the future, understand the decision in this case to be based on such evidence. This is because the Federal Circuit relied solely on "GE's own technical literature [that] emphasized the MAO feature" (Pet. App. 15a); quoting from only three GE brochures, the lower court held that "[t]here was thus substantial evidence to support an award of a reasonable royalty based upon the cost of the entire accused machines." *Id.* at 16a.

In all events, even the evidence that Fonar cites is plainly not enough to establish that, in the absence of such a feature, the machine is commercially "worthless" (*Crosby Steam-Gage & Valve Co.* v. *Consolidated Safety-Valve Co.*, 141 U.S. 441, 453 (1891) (internal quotation omitted)) or devoid of practical utility (*Marconi Wireless*, 99 Ct. Cl. at 48). Indeed, any such conclusion is foreclosed by the facts of record that the feature was only one of many options on Fonar scanners, that even those customers who have the feature use it only half the time, and that GE scanners without the feature outsold Fonar scanners with it five-to-one—facts that Fonar does not and cannot dispute. Pet. 6, 14-15; Opp. 4.[6] Accordingly, the entire

[6] Fonar's factual assertions (Opp. 13-14) are misleading for additional reasons. Although the MAO feature became standard on all GE machines in 1992, Fonar itself offered the MAO feature

market value rule, as this Court articulated it, could not have been satisfied here.[7]

Although Fonar is completely unable to rebut GE's showing that the Federal Circuit has progressively abandoned the entire market value rule that this Court developed (Pet. 12-13), Fonar asserts that this Court's denial of certiorari in *Rite-Hite* should control the result here. Opp. 15 n.5. But this case is a substantially better vehicle than *Rite-Hite* because it involves the more "typical[]" case when "unpatented and patented components are physically part of the same machine," (*Rite-Hite*, 56 F.3d at 1549); and because the patentee in *Rite-Hite* could not satisfy even the plurality's diluted version of the rule, which is why Judge Nies was able to "agree [with the result] . . . that under the entire market value rule, Rite-Hite is not entitled to lost profits on dock levelers." *Id.* at 1575. Moreover, as the *amicus* brief of the Intellectual Property Owners demonstrates, the Federal Circuit's inability to provide clear guidance in *Rite-Hite* has spawned fur-

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as an "option," which a significant number of its customers declined. C.A. App. A7178; *id.* at A7334-39; *cf. id.* at A5417-18. The assertion that GE standardized the feature because it faced a competitive threat from Fonar is absurd given that Fonar's sales steadily declined during the three years prior to 1992—from a high of 23 in 1989, to 16 in 1990, to 5 in 1991. *Id.* at A5102-06. GE's scanner without MAO not only outsold Fonar's scanners five-to-one during this three-year period, but even after GE discontinued that model, GE was still able to sell used systems without any MAO feature. *Id.* at A5191. Such facts confirm that MAO did not drive customer demand for scanners any more than right-side mirrors (now standard on new cars) drive the demand for cars.

[7] Implicitly recognizing this, Fonar suggests that the issue GE seeks to raise is not presented because GE did not object to the jury instructions below. Opp. 11. But, as this Court has explained, "[i]f the evidence presented [at trial] would not suffice, as a matter of law, to support a jury verdict under the [correct standard], judgment could properly be entered" in favor of a defendant notwithstanding its failure to object to an incorrect jury instruction. *Boyle* v. *United Techs. Corp.*, 487 U.S. 500, 513-14 (1988); *see also City of St. Louis* v. *Praprotnik*, 485 U.S. 112, 120 (1988) ("failure to object to an instruction does not render the instruction the 'law of the case' " for purposes of appeal) (plurality opinion)).

ther confusion and inconsistency in this area of law, with district courts applying three different standards. See Brief of *Amicus Curiae* of Intellectual Property Owners in Support of Certiorari at 8-12.

Finally, in response to GE's demonstration of widespread criticism both within and outside the Federal Circuit of its loosening of the traditional restriction embodied in the entire market value rule (see Pet. 13, 17), Fonar only feebly asserts that those criticisms were directed at "applications" of the rule involving items "physically distinct" from the patented device. Opp. 15. This is not true. In *King Instrument Corp.* v. *Perego,* 72 F.3d 855 (Fed. Cir. 1995), *cert. denied,* 116 S. Ct. 1675 (1996), where, as here, the "patented invention [was] a component of a device" and not physically separate from it, Judge Nies *again* denounced as a "perversion of patent infringement damages" the Federal Circuit's refusal to require proof of damages "in accordance with the 'entire market value rule.' " *Id.* at 856, 857. In her view, *King Instrument* confirmed that "the *Rite-Hite* decision was not an aberration" but a "profound departure" from traditional patent law. *Id.* at 857. Indeed, Judge Nies could "only conclude that in denying *certiorari* [in *Rite-Hite*], the Supreme Court had not been made aware of the significance of the fundamental change in patent rights made by the *Rite-Hite* decision." *Id.* Fonar fails to offer any logical or policy reason why this Court should not review such a significant departure from its previously established rules.

II.

As to GE's second question, Fonar principally asserts that the court of appeals did not address whether particularized testimony and linking argument (see Pet. 4) is needed to sustain a verdict based on the doctrine of equivalents because "the equivalents issue was front and center at every stage of the trial." Opp. 18. It is true that the jury received generic opening instructions and jury instructions that mentioned the theory of equivalents. But Fonar does not and cannot cite a single piece of evidence or linking argument at the trial that sets forth the novel theory of

equivalent infringement that Fonar advanced in its reply brief on appeal and that the panel accepted wholesale. Absent such crucial evidence and argument, judicial resort to the doctrine of equivalents to affirm a jury verdict is irreconcilable with the limits that *Hilton-Davis* recognized must be established and enforced if the doctrine of equivalents is not to continue to have "a life of its own." *Warner-Jenkinson Co.* v. *Hilton-Davis Chem. Co.*, 117 S. Ct. 1040, 1048-49 (1997).

The third step of the '832 patent calls for a comparison of the relaxation times measured in step B with the standard values established in step A. Pet. 6-7. Only in its reply brief did Fonar advance the theory that the comparison step occurred *before* the visualization of the image by the physician, when the "signal strength" of a voxel allegedly "was matched to a value within precalibrated gray scale values." Pet. App. 22a. Assuredly, if Fonar could have found a single passage when its witness or counsel argued that the comparison step occurred internally in the MRI scanner, before the physician saw the image, Fonar would have quoted it. There is no such citation because there is no such evidence.[8]

Indeed, neither Fonar's counsel nor Dr. Damadian ever provided the jury with Fonar's reply brief theory of equivalence. The theory of comparison that the jury actually heard was that the comparison step occurs when the physician looks at the MRI image where the "brightness" of the suspect tissue "is set off from" the relatively darker "surrounding tissue." See C.A. App. A3239; see also Fed. Cir. Fonar Br. 47 ("the *viewer* of the image makes an *optical comparison measurement*" of the relative "brightness" of adjacent tissues) (emphasis added). Fonar abandoned

[8] Apart from generic jury instructions on equivalence, all that Fonar can cite is (1) Dr. Damadian's analogies that purported to establish that the *second* step—the measuirng of T_1 and T_2 values of suspect tissue—takes place in a scanner, and (2) counsel's plainly irrelevant statement in closing argument about "signal intensity formulas" that serendipitously uses the word "equivalent." Opp. 19-20.

that theory in its reply brief because it is squarely foreclosed by the plain language of the patent as well as the Federal Circuit's prior and binding claim construction in *Johnson & Johnson*. See Pet. 7.

Apart from a false statement about waiver,[9] Fonar's only other defense of the panel's unbounded application of the doctrine of equivalents is that the author of the opinion below has previously applied the rule of particularized testimony and linking argument. But this only further underscores why this Court should accept this issue: Panels within the Federal Circuit openly dispute whether the *Nestier* rule should apply. See Pet. 18. Because the Federal Circuit, even after *Hilton-Davis*, has not set and enforced a vital procedural limit on the use of the doctrine of equivalents, plenary review by this Court is warranted.

CONCLUSION

For the reasons stated above and in the petition, the petition should be granted.

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[9] Contrary to Fonar's inexplicable misrepresentation (Opp. 17 n.8), GE explicitly moved both at the close of trial (C.A. App. A4820-21), and after the verdict (*id.* at A1014-15), to take the issue of infringement of the '832 patent from the jury, which the Federal Circuit has held is sufficient to preserve an objection to a lack of particularized testimony and linking argument under the doctrine of equivalents. *Malta* v. *Schulmerich Carillons, Inc.*, 952 F.2d 1320, 1324-25 (Fed. Cir. 1991).

Respectfully submitted,

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